Office - Supreme Court, U.
FILED
FEB 10 1953
HAROLD B. WILLEY, C

No. 597

Petition for Certiorari

In the

Supreme Court of the United States

OCTOBER TERM, 1952

CHRIS C. MALETIS, *Petitioner*

vs.

UNITED STATES OF AMERICA, *Respondent*

Petition for a Writ of Certiorari To the United States Court of Appeals For the Ninth Circuit

GEORGE BLACK, JR.
Counsel for Petitioner

DAILY JOURNAL OF COMMERCE

INDEX

	PAGE
Opinions below	1
Jurisdiction	2
Question presented	2
Statutes involved	2
Statement	2
Reasons for granting the writ	5
Conclusion	9

CITATIONS

CASES:

Commissioner of Internal Revenue v. *Tower*, 327 U. S. 280 3

Higgins v. *Smith*, 308 U. S. 473 ..... 6, 7

Lusthaus v. *Commissioner of Internal Revenue*, 327 U. S. 293 3

STATUTES:

Internal Revenue Code §§ 22(a), 23(s), 122 and 3797 (26 U.S.C. 1946 ed. §§ 22(a), 23 (s), 122 and 3797 2

MISCELLANEOUS:

I.T.-3845, 1947-1 Cum. Bull. 66 2

APR 22 1954

205391

In the

Supreme Court of the United States

OCTOBER TERM, 1952

CHRIS C. MALETIS, *Petitioner*

vs.

UNITED STATES OF AMERICA, *Respondent*

Petition for a Writ of Certiorari To the United States Court of Appeals For the Ninth Circuit

---

Petitioner, Chris C. Maletis, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in the above entitled case on November 17, 1952.

OPINIONS BELOW

The opinion of the United States District Court for the District of Oregon (R. 28) is reported in 97 Fed. Sup. 562.

The opinion of the United States Court of Appeals for the Ninth Circuit (R. 142) is reported in 200 F. 2d 97.

JURISDICTION

The judgment of the United States Court of Appeals for the Ninth Circuit was entered November 17, 1952 (R. 146). The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

QUESTION PRESENTED

Are the tax laws of the United States of America, and especially those involving the recognition of family partnerships, to be applied in one way when they may benefit the Government and in another way when they may benefit the taxpayer?

STATUTES INVOLVED

Sections 22(a), 23(s), 122 and 3797 of the Internal Revenue Code as amended (26 U.S.C. 1946 ed. §§ 22(a), 23(s), 122 and 3797) U.S. Treasury Regulations thereunder and I.T. 3845, 1947-1 Cum. Bull. 66 are involved.

STATEMENT

Taxpayer Malotis, petitioner herein, was a sole proprietor engaged in distributing beer and wine. For the purpose of supplementing his stock of wine he bought the equipment of a berry winery in 1943. In 1945 he executed a partnership agreement with his two sons for the purpose of continuing to conduct the winery business. One of the boys was a minor (R. 103) and away at school. The other was away in the army (R.

120). Taxpayer desired to make some money for his boys and felt that the partnership arrangement, good under state law, was similarly good for federal income tax purposes, even though, as the facts clearly appear, the boys had no money or credit or skill and furnished no capital and performed no services and did not participate in the control or management of the business, and that all matters relating to financial transactions, operations and the profit or loss in the business were actually handled by the father himself, who continued to dominate and control the business (R. 103, 105, 107, 108, 109, 113, 120, 121, 123, 124, 126).

Subsequently, and in 1946, the cases of *Commissioner of Internal Revenue v. Tower*, 327 U. S. 280, and *Lusthaus v. Commissioner of Internal Revenue*, 327 U. S. 293, were decided. As a result, for the first time there were some accepted and recognized tests for determining what was a partnership within the meaning of the tax law.

An Internal Revenue Agent, checking the year 1945, advised the Taxpayer that said partnership, even though good under state law, did not qualify as a partnership under federal tax law, and demanded that profits earned by said winery partnership be entirely included in Taxpayer's 1945 personal return. It thereafter also appeared that said winery venture had suffered an operating loss

in excess of $100,000 during the calendar year 1947. Through loss carry-back, Taxpayer was then actually entitled to a substantial refund on the very large personal income taxes that he had theretofore paid for 1945.

Appropriate accounting changes and returns were made and Taxpayer-Petitioner filed claim for the net refund due him (giving the Government all appropriate credits on the re-adjustment) as a result of the loss carry-back. Denial of the refund application resulted in this lawsuit.

The Commissioner has taken the position that the Taxpayer cannot be permitted now to say that this venture did not qualify for a partnership under federal law, rules and regulations, regardless of whether it did or did not so qualify. The Court of Appeals sustained the Commissioner's position, holding that the Government may apply or withhold its tests and regulations for determination of whether a federal income tax partnership exists, according to how *it feels* the tax statute will be best served.

The elements of estoppel do not exist here. There is no change in any facts or representation of facts. There is no reliance by the Government, or change of the Government's position, or injury to the Govenrment.

REASONS FOR GRANTING THE WRIT

The decision of the lower court rendered herein involves an important question of federal law which has not been and which should be, settled by this Court. That question, in the ultimate, is whether the tax laws of the United States of America are to be applied in one way when they benefit the Government an another way when they benefit the taxpayer.

It is clear from all the facts and evidence in this case, that, were the Taxpayer attempting to sustain the validity of this partnership for tax purposes, the courts would have no hesitancy in overruling his contention under the applicable criteria and tests. Taxpayer would have been required to report *all* income therefrom as his own. Nonetheless, the decision of the lower court permits that Taxpayer to report only *one-third* of the loss as his own. This introduces a concept of *double standards* into the law.

When Taxpayer proceeded to place his house in order, pursuant to the established regulations, criteria and tests, and found, to his surprise and to the consternation of the Commissioner, that he would be entitled to a substantial refund, the Commissioner then refused to apply those very tests which are otherwise employed in determining whether or not a given partnership will qualify for federal income tax purposes. There has

never been an expression by this Court as to whether the validity of a partnership, for federal income tax purposes, is to be determined by the application of the same tests regardless of whether the taxpayer or the Government is seeking the determination. This Court is now being requested, for the first time, to dispel this confusion and to recognize and announce the principle that the tax laws of the United States, and particularly those involving the recognition of family partnerships, are to be applied in the same manner, regardless of whether the application thereof may be to the benefit of the Government or to the benefit of the taxpayer.

It is, we believe, plainly in the public interest for this Court to annuonce that inasmuch as this venture would not have qualified as a partnership for federal income tax purposes had it proven profitable, it does not qualify any the more as such a partnership simply because it suffered losses.

The Court of Appeals asserts the opinion that Taxpayer "elected" to do business as a partnership and is therefore now barred from disclaiming the validity of said partnership for income tax purposes. It cites language from the case of *Higgins v. Smith*, 308 U. S. 473, in support of its apparent position that, in a situation of this kind, the Treasury Department can, in its discretion, apply or withhold its established regulations, stand-

ards and tests for the recognition of a partnership for income tax purposes.

Reference by the Court of Appeals to an "election" on the part of this Taxpayer is erroneous. Taxpayer did not have any choice available to him. Therefore, there is no election involved. Under the facts applicable to his partnership and the applicable federal income tax law, Taxpayer did not have two courses of action available to him, one of which would have resulted in a partnership recognizable for tax purposes and the other of which would not have been so recognizable.

Whether or not one has a partnership which is acceptable for federal income tax purposes, is a legal conclusion, to be arrived at only after examining the facts in the light of applicable principles. What the Taxpayer has may be a partnership or it may be an individual proprietorship. He has no option, and there is no choice. An erroneous legal opinion of the Taxpayer as to whether his form of business is a proprietorship or a partnership for federal income tax purposes, is no "election" by him. We submit that there is no doctrine of election applicable in this case.

The *Higgins* case did not involve family partnership nor did it involve a situation at all similar to the instant case. The language which the Court of Appeals quotes from the *Higgins* case is not applicable to the

instant situation. There is no election here. There is no fiction here, and there is no sham here. The instant case points up in bold type the various interpretations and applications which are being made as a result of the highly confused rules concerning the recognition of a family partnership for tax purposes. It took a long time for the Treasury Department to find out what was a good family partnership and what was a bad one. But once it settled upon the regulations, rules and tests, application thereof should be made the same, regardless of whether the result is favorable to the Government or the taxpayer.

The doctrine asserted by the Court of Appeals is a dangerous one. It is not in accord with our system of jurisprudence and the relations between the Government and its citizens that the Treasury Department be given such discretionary power to extend or withhold relief in a situation of this kind. There is a spirit of fair play that runs throughout our entire jurisprudence. This spirit should be preserved. It requires that the rules of the game work both ways.

Public confidence in the administration of the tax laws in this country is important. Such confidence would be materially aided if this Court would reverse the decision of the Court of Appeals in this case and repudiate the doctrine which its opinion asserts.

CONCLUSION

For the foregoing reasons, this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

GEORGE BLACK, JR.

Counsel for Petitioner.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute involved	2
Statement	2
Argument	4
Conclusion	6
Appendix	7

CITATION

Cases:

Commissioner v. *Culbertson*, 337 U.S. 733	5, 6
Commissioner v. *Tower*, 327 U.S. 280	6
Higgins v. *Smith*, 308 U.S. 473	5
Love v. *United States*, 96 F. Supp. 919	5
Lusthaus v. *Commissioner*, 327 U.S. 293	6
Moline Properties v. *Commissioner*, 319 U.S. 436	5
Phillips v. *United States*, 193 F. 2d 132	5

Statute:

Internal Revenue Code:	
Sec. 23 (26 U.S.C. 1946 ed., Sec. 23)	7
Sec. 122 (26 U.S.C. 1946 ed., Sec. 122)	7
Sec. 181 (26 U.S.C. 1946 ed., Sec. 181)	9
Sec. 182 (26 U.S.C. 1946 ed., Sec. 182)	9
Sec. 187 (26 U.S.C. 1946 ed., Sec. 187)	9
Sec. 189 (26 U.S.C. 1946 ed., Sec. 189)	10

In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 597

CHRIS C. MALETIS, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 28-33) is reported in 97 F. Supp. 562. The opinion of the Court of Appeals (R. 142-145) is reported in 200 F. 2d 97.

JURISDICTION

The judgment of the Court of Appeals was entered on November 17, 1952. (R. 146.) The petition for a writ of certiorari was filed on February 10, 1953. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether the taxpayer is entitled to carry back and deduct from his income for one year, as his individual loss, the entire net operating loss sustained during a later year by a business which he and his sons organized and operated as a family partnership, but which the taxpayer now asserts was, for tax purposes, his sole proprietorship.

STATUTE INVOLVED

The pertinent provisions of the statute involved are printed in the Appendix, *infra*, pp. 8-11.

STATEMENT

The facts as found by the District Court (R. 47-53) may be summarized as follows:

On April 18, 1945, the taxpayer and his two sons entered into a written partnership agreement for the manufacture and sale of wines under the name of "Maletis & Sons", the profits and losses therefrom to be distributed in equal proportions. The initial capital of $9,000 was supplied by Alta-Chris, a family partnership consisting of the taxpayer and his wife. (R. 48-49.) The taxpayer admits that the partnership agreement is valid under the state law. (R. 7.)

At the time of the execution of the partnership agreement and at all material times thereafter, both sons were either in the Army or attending school, and were dependent upon the taxpayer for their support and maintenance. Neither son had any money or credit of his own and, with the ex-

ception of the initial capital, all the money and credit supplied for the partnership originated with the taxpayer. (R. 49.) The taxpayer had little, if any, and his sons had no experience in the manufacture of wines. During the life of the partnership, the sons' activities were limited to the signing of documents and checks. (R. 49.)

Partnership income returns were duly filed, showing the distributive share of the three partners in net income of $15,275:69 for the fiscal year ended April 30, 1946, and a net loss of $11,371.14 for the fiscal year ended April 30, 1947. (R. 50, 51, 53.) On or about May 15, 1946, the taxpayer filed his federal income tax return for the calendar year 1945, showing therein a tax liability of $228,925.28, which was duly paid. (R. 50.)

On or about March 2, 1948, the taxpayer filed his separate individual income tax return for the calendar year 1947, reporting an alleged loss of $93,205.61 and no tax due. He claimed therein that the partnership had sustained a loss of $112,093.37 for the calendar year 1947, that it was invalid for tax purposes because it was his sole proprietorship, and that the loss, after making certain adjustments, was deductible from his individual income. (R. 51-52.) At the same time, the taxpayer filed a claim for refund of $64,564.86 income tax paid by him for 1945, on the same ground that the partnership was invalid for tax purposes, and that he was, therefore, entitled, under Sections 23(s) and 122 of the Internal Revenue Code, to the deduction of $93,205.61 from his income for

that year as his individual net operating loss carry-back from the year 1947. (R. 52.)

The district court expressly found that when the partnership agreement was executed and at all times during its continuation, the taxpayer and each of his two sons had a *bona fide* intention to form and operate a partnership. (R. 53.)

Upon the basis of these facts, the district court held that the partnership must be recognized as real for income tax purposes, and therefore the taxpayer's claim that he alone, exclusive of the other partners, is entitled to have the entire amount of the partnership's net operating loss for the calendar year 1947 applied as a carry-back deduction against his individual income for the calendar year 1945, as his individual loss, must be rejected. (R. 28-33, 53-54.) The Court of Appeals affirmed. (R. 142-145.)

ARGUMENT

This case presents no question calling for review by this Court. No conflict of decisions is involved; nor, contrary to the taxpayer's contention (Pet. 5), does the case raise any question of federal law of general importance. The reasons asserted by the taxpayer for allowance of the writ relate to the merits, and were asserted below; and the opinions of both lower courts show that the case was correctly decided.

The taxpayer now asserts that the partnership formed by him and his sons was not a valid one for tax purposes, and that the question is whether the tax laws of the United States are to be applied

in one way when they benefit the Government and in another way when they may benefit the taxpayer. (Pet. 2, 5.) This begs the real issue. The point of this case is that the taxpayer, upon adopting the partnership form of organization with his two sons and having elected to carry on the winery business as a partnership for several years, may not thereafter disavow the validity of such business arrangement in order to escape disadvantageous tax consequences in later years, upon the asserted ground that the arrangement was unreal or a sham.

Both courts below so held, and their conclusions are in accord with *Higgins* v. *Smith*, 308 U.S. 473, 477. Cf. *Moline Properties* v. *Commissioner*, 319 U.S. 436, 439. As summarized by the Court of Claims in *Love* v. *United States*, 96 F. Supp. 919, 921, "the taxpayer may not escape the tax consequences of a business arrangement which he made upon the asserted ground that the arrangement was fictional." See also *Commissioner* v. *Culbertson*, 337 U.S. 733, 753, stating, on the authority of *Higgins* v. *Smith*, *supra*, p. 477, that the taxing authorities may properly insist on "holding the taxpayer to his election to adopt the form of a partnership." Cf. *Phillips* v. *United States*, 193 F. 2d 132 (C.A. 5th).

The district court found (R. 53) in this case that, as they testified (R. 81-82, 96, 116, 126-127), the taxpayer and both of his sons really intended in good faith to enter into a genuine partnership arrangement and thereafter to carry on the busi-

ness. *Commissioner* v. *Culbertson, supra,* p. 742. The taxpayer suggests that this Court's decisions in *Commissioner* v. *Tower,* 327 U.S. 280, and *Lusthaus* v. *Commissioner,* 327 U.S. 293, constituted the purported reason for his thereafter renouncing the partnership here and claiming its entire loss as his individual loss carry-back deduction for 1945 (Pet. 2-4). The record shows, however, that he first disavowed the partnership in March, 1948, when it became apparent that its large 1947 loss could benefit only him as a carry-back loss deduction for 1945. (R. 51-52.) The *Tower* and *Lusthaus* cases were decided on February 25, 1946.

CONCLUSION

The decision below is correct. It turns on the particular facts of this case, and there is no conflict of decisions. The petition for a writ of certiorari should be denied.

Respectfully submitted,

ROBERT L. STERN,
Acting Solicitor General.

H. BRIAN HOLLAND,
Assistant Attorney General.

ELLIS N. SLACK,
ROBERT N. ANDERSON,
S. DEE HANSON,
Special Assistants to the Attorney General.

MARCH, 1953.

APPENDIX

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(s) [As added by Sec. 211 (a), Revenue Act of 1939, c. 247, 53 Stat. 862] *Net Operating Loss Deduction.*—For any taxable year beginning after December 31, 1939, the net operating loss deduction computed under section 122.

(26 U.S.C. 1946 ed., Sec. 23.)

SEC. 122 [As added by Sec. 211 (b), Revenue Act of 1939, *supra*]. NET OPERATING LOSS DEDUCTION.

(a) [As amended by Sec. 105 (e) (3) (A), Revenue Act of 1942, c. 619, 56 Stat. 798] *Definition of Net Operating Loss.*—As used in this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

(b) [As amended by Sec. 153 (a), Revenue Act of 1942, *supra*] *Amount of Carry-Back and Carry-Over.*—

(1) *Net operating loss carry-back.*—If for any taxable year beginning after December 31, 1941, the taxpayer has a net operating loss, such net operating loss shall be a net

operating loss carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the second preceding taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such second preceding taxable year without regard to such net operating loss.

* * * * *

(c) [As amended by Sec. 153 (b), Revenue Act of 1942, *supra*] *Amount of Net Operating Loss Deduction.*—The amount of the net operating loss deduction shall be the aggregate of the net operating loss carry-overs and of the net operating loss carry-backs to the taxable year reduced by the amount, if any, by which the net income (computed with the exceptions and limitations provided in subsection (d) (1), (2), (3), and (4)) exceeds, in the case of a taxpayer other than a corporation, the net income (computed without such deduction)
* * *

(d) [As amended by Sec. 105 (e)(3)(C), Revenue Act of 1942, *supra*] *Exceptions, Additions, and Limitations.*—The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

* * * * *

(3) No net operating loss deduction shall be allowed;

(4) [As amended by Sec. 150 (e), Revenue Act of 1942, *supra*] Gains and losses from sales or exchanges of capital assets shall be taken into account without regard to the provisions of section 117 (b). As so computed the amount deductible on account of such losses shall not exceed the amount includible on account of such gains.

* * * * *

(26 U.S.C. 1946 ed., Sec. 122.)

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

(26 U.S.C. 1946 ed., Sec. 181.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b)

(26 U.S.C. 1946 ed., Sec. 182.)

SEC. 187. PARTNERSHIP RETURNS.

Every partnership shall make a return for each taxable year, stating specifically the items

of its gross income and the deductions allowed by this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe, and shall include in the return the names and addresses of the individuals who would be entitled to share in the net income if distributed and the amount of the distributive share of each individual. The return shall be sworn to by any one of the partners.
(26 U.S.C. 1946 ed., Sec. 187.)

SEC. 189 [As added by Sec. 211 (d), Revenue Act of 1939, *supra*]. NET OPERATING LOSSES.

The benefit of the deduction for net operating losses allowed by section 23 (s) shall not be allowed to a partnership but shall be allowed to the members of the partnership under regulations prescribed by the Commissioner with the approval of the Secretary.
(26 U.S.C. 1946 ed., Sec. 189.)

☆ U. S. GOVERNMENT PRINTING OFFICE: 1953 244886 1240